CANADIAN PIONEER OILS LTD.

1986 annual report

Canadian Pioneer Oils Ltd.

Corporate Profile

Canadian Pioneer Oils Ltd. is a Canadian, Calgary based, public oil and gas Corporation listed on the Alberta Stock Exchange. Incorporated in Alberta in 1978, the Corporation is engaged in the exploration, development, production and acquisition of oil and gas in Canada and the United States. At June 30, 1986, the Corporation had 10,890,277 Class A Common Shares and 29,000 First Preference Shares outstanding. Northgate Exploration Limited, a Canadian public mining corporation, is the major shareholder, owning 8,051,856 shares (74%).

Highlights of the 1986 Fiscal Year

Financial ($000 except per share amounts)

	1986	1985
Production revenue	**$ 2,786**	$ 3,056
Cash flow	**$ 778**	$ 1,029
per share	**$ 0.07**	$ 0.10
Net earnings (loss)	**$ (2,181)**	$ 328
per share	**$ (0.21)**	$ 0.03
Capital expenditures	**$ 1,631**	$ 1,271
Book value of assets	**$10,197**	$11,984
Long term debt	**$ 5,400**	$ 6,150
Shareholders' equity	**$ 3,135**	$ 4,947
Number of common shares outstanding	**10,890,277**	10,454,947

Operating

	1986	1985
Production		
Oil — barrels	**25,986**	30,583
— barrels per day	**71**	84
Gas— thousand cubic feet	**866,995**	783,114
— thousand cubic feet per day	**2,375**	2,146
Reserves (proven and probable)		
Oil — barrels	**306,900**	293,500
Gas— thousand cubic feet	**16,263,500**	17,040,000

Notice of Annual Meeting

The Annual Meeting of Shareholders will be held at the Westin Hotel, 4 Ave. & 3 St. S.W., Calgary, Alberta, on December 9th, 1986 at 10 A.M. in the Lougheed Room.

Abbreviations

Throughout this report standard oil and gas abbreviations have been used as follows:

MSTB	Thousand Stock Tank Barrels
BOPD	Barrels of Oil per Day
BCF	Billion Cubic Feet
MCFD	Thousand Cubic Feet per Day
D&A	Dry and Abandoned

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Report to Shareholders

The Board of Directors is pleased to present the Annual Report of Canadian Pioneer Oils Ltd. for the year ending June 30, 1986. The Corporation had a satisfactory year, despite the difficult environment created by sharply lower oil prices in the last half of the year and the continued softening of natural gas prices.

Production revenues decreased 9% to $2,786,000 in 1986 from $3,055,000 in 1985. The decrease in revenue was not as severe as the fall in world oil prices due to the fact that the major part of Canadian Pioneer's revenue is derived from gas sales. The Corporation's United States assets were written down by $2,593,000 in 1986 and this write down was the main contributing factor in a net loss for the year of $2,181,000 ($0.21 per share). Operating cash flow was $778,000 in 1986 compared to $1,029,000 in 1985.

Gas production increased to 2,375 thousand cubic feet per day compared to 2,146 thousand cubic feet per day in 1985. Several new gas wells were placed on production in the Birch Wavy area of Alberta. Oil production declined from 84 to 71 barrels of oil per day, mainly due to pro-rationing of the Corporation's light gravity oil production in Northern Alberta and the temporary shut in of the Glenevis oil property to implement a cost saving water disposal facility. New oil wells were placed on production in the Lochend, Lubicon and Otter areas of Alberta.

The Corporation's proven and probable reserves at year-end were estimated at 306,900 barrels of oil and 16.3 billion cubic feet of gas. Approximately 70% of the oil and gas reserves are proven. Oil reserves were up 5% and gas reserves were down 4% compared to the previous year.

Canadian Pioneer participated in the drilling of 31 wells during the year. Drilling was undertaken for gas in the Trochu and Birch Wavy areas of Alberta, and for oil in the Otter and Lubicon areas of Alberta. Eighteen wells were also drilled in various areas of Alberta on a farmout basis at no capital cost to Canadian Pioneer. The drilling resulted in eight oil wells and 12 gas wells being completed and the Corporation plans to continue to pursue similar high quality prospects in 1987.

Canadian Pioneer is reacting to declining oil and gas prices and reduced revenues by taking measures to ensure an efficient operation that will maximize cash flow. Long term debt was reduced from $6,150,000 at June 30, 1985 to $5,400,000 at June 30, 1986 and general and administrative expenses have also been reduced. New gas contracts are being pursued in order to maximize deliverabilities and utilize the productive capacity of the Corporation's gas reserves.

The coming year will be a difficult one for all companies in the oil and gas industry. However, Canadian Pioneer is encouraged by the recent announcement of the Alberta Government to reduce royalties and extend the royalty rebate program for small producers to December, 1987. With gas deregulation occurring on November 1, 1986, Canadian Pioneer is optimistic that new markets will be created which the Corporation plans to pursue and is already negotiating a gas contract for sales to the United States.

The Corporation acknowledges with appreciation the contribution of management and staff during a difficult year. It is with regret that the untimely death is recorded of Ronald R.J. Derouin in January, 1986 as a result of a motor vehicle accident. Mr. Derouin had been President and Chief Operating Officer of the Corporation since December 1984. Mr. John F. Kearney, Chief Executive Officer of the Corporation was appointed acting President.

October 31, 1986


RAINBOW
Sixth Meridian
Fifth Meridian
Fourth Meridian
120
110
80
70
60
50
40
30
20
10
10
20
10
20
10
20
10
ALBERTA
EDMONTON
PLAIN
STROME
TROCHU
HARMATTAN
EAST
CALGARY
MAJOR
PROPERTIES
TOWNSHIPS IN WHICH
CANADIAN PIONEER
HAS HOLDINGS

Exploration and Development

Canadian Pioneer continued its exploration philosophy in 1986 by participating in prospects in areas that provide high quality multiple reservoir potential with low to medium risks. Gas prospects drilled were located in Central Alberta close to pipelines and facilities. The oil prospects were for light gravity oil with high producing potential. The Corporation plans to continue to pursue similar high quality prospects in 1987 so as to maintain the highest possible netbacks from the petroleum products produced.

Land Activity

The Corporation acquired 4,525 gross acres (2,672 net acres) and expended $99,000 on land during the year. The principal areas of interest were in the Trochu and Birch Wavy areas of central Alberta.

Canadian Pioneer has concentrated much of its efforts in developing a substantial acreage position in the Trochu area where five wells have been drilled on Corporation lands. The Corporation now has 5,915 gross acres (4,304 net acres) in the Trochu area. In the Birch Wavy area, 1,195 gross acres (342 net acres) were acquired to allow for the completion of spacing units.

Canadian Pioneer's land holdings are as follows:

	1986		1985	
	Gross Acres	Net Acres	Gross Acres	Net Acres
Canada	199,112	45,770	217,334	49,948
United States	75,419	3,746	77,282	4,678
TOTAL	274,531	49,516	294,616	54,626

Drilling Activity

Despite the downturn in the industry during fiscal 1986, drilling activity on Canadian Pioneer lands continued at the same level as the previous year with the Corporation participating in 31 wells. In Canada 28 wells were drilled, including 17 on a farmout basis, resulting in eight oil wells and ten gas wells. In the United States three wells were drilled on a farmout basis resulting in two producing gas wells.

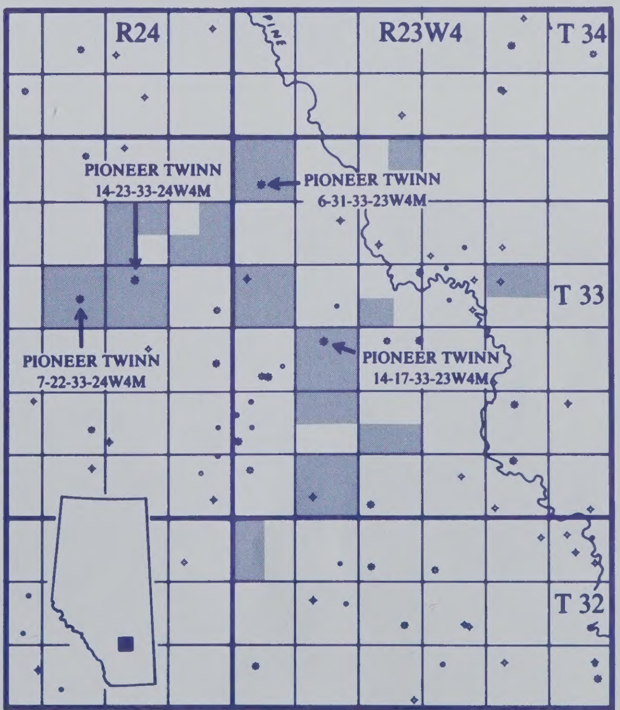
WELLS DRILLED

	Canada			United States			
Fiscal Year	Oil	Gas	D&A	Oil	Gas	D&A	Total
1982	2	19	4	3	—	2	30
1983	—	22	6	2	—	2	32
1984	—	7	4	3	—	1	15
1985	6	10	11	2	1	1	31
1986	8	10	10	—	2	1	31

In the Trochu area of Alberta, the Corporation has participated at an average 41% working interest in five Banff tests which were drilled for multiple potential gas zones. The drilling program has resulted in three completed gas wells and one potential gas well. The Corporation is currently seeking a market for this gas and will tie-in several of the gas wells for production beginning in late 1986 if a gas contract is finalized for the Trochu area. Further development drilling in this area is dependent on economics and demand for gas from future gas contracts.

The Corporation's land holdings in East Central Alberta continued to be developed in 1986 primarily through farmouts. Nine wells were drilled in this area resulting in five gas wells. The gas is contracted to TransCanada Pipelines and two of the gas wells will be placed on production in November, 1986.

Canadian Pioneer continues to hold acreage in the Joffre and Clive areas of Central Alberta that is prospective for Nisku and Leduc reef potential. In the Joffre area the Corporation owns a 12.5% interest in lands immediately adjacent to the recently announced 3,000 barrels of oil per day Leduc oil discovery by ICG Resources Ltd. Geophysical evaluation is needed to further define potential for this acreage. It is anticipated this work will be performed in 1987.



TROCHU AREA, Alberta

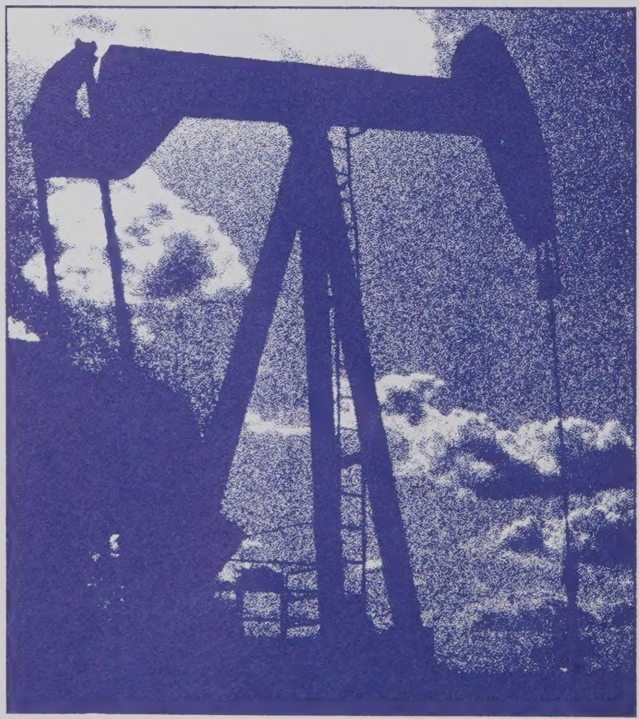
CANADIAN PIONEER Land
Location
Oil Well
Gas Well
Oil & Gas Well
Dry & Abandoned Well
Abandoned Oil/Water Injection

Production and Operations

Canadian Pioneer realized an increase in gas production to 867 million cubic feet (2,375 thousand cubic feet per day) in 1986 from 783 million cubic feet (2,146 thousand cubc feet per day) in 1985. The higher gas production was due to increased demand and new wells being placed on production. Oil production for 1986 was 25,986 barrels (71 barrels of oil per day) compared to 30,583 barrels (84 barrels of oil per day) for 1985. The decrease was mainly the result of reduced nominations on the Corporation's light oil properties and the temporary shutting in of the Glenevis oil property for installation of water disposal facilities designed to reduce operating costs.

During 1986 the Corporation placed two gas wells on production in the East Central area of Alberta. Five oil wells were placed on production during the year, four in the Lubicon-Otter area and one in the Lochend area of Alberta.

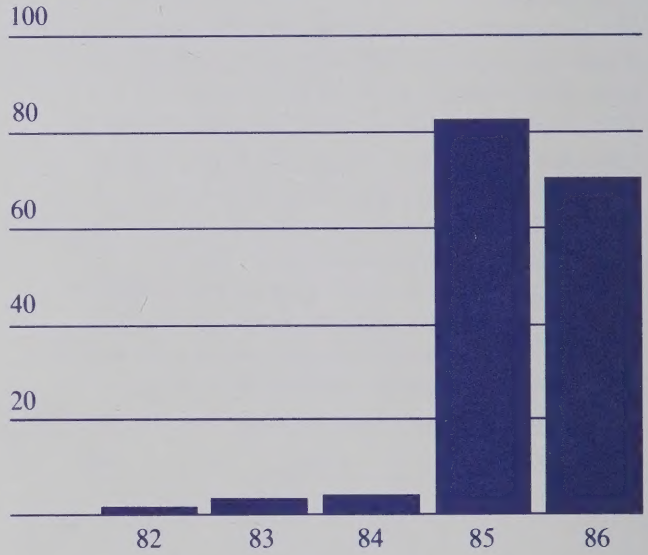
The Garrington oil property, which was Canadian Pioneer's largest oil producing property has now been included in the newly formed Harmattan East Viking Unit No. 1. Canadian Pioneer has a 0.9% working interest in the Unit which is projected to produce in excess of 3,000 barrels per day under a waterflood scheme that has been implemented to increase ultimate oil recovery.



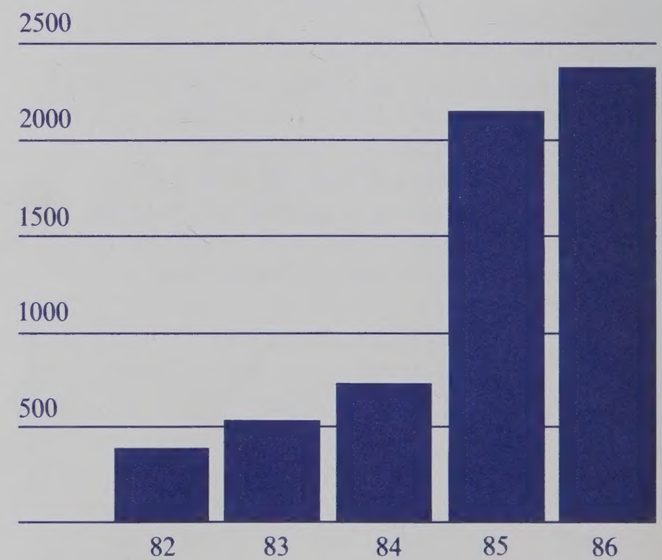
In the United States, production for the year was 121 million cubic feet of gas (331 thousand cubic feet per day) and 4,300 barrels of oil (12 barrels per day).

At June 30, 1986, the Corporation had 128 producing wells including 26 oil and 47 gas wells in Canada and 17 oil and 38 gas wells in the United States.

Oil Production (bopd)



Gas Production (mcfd)

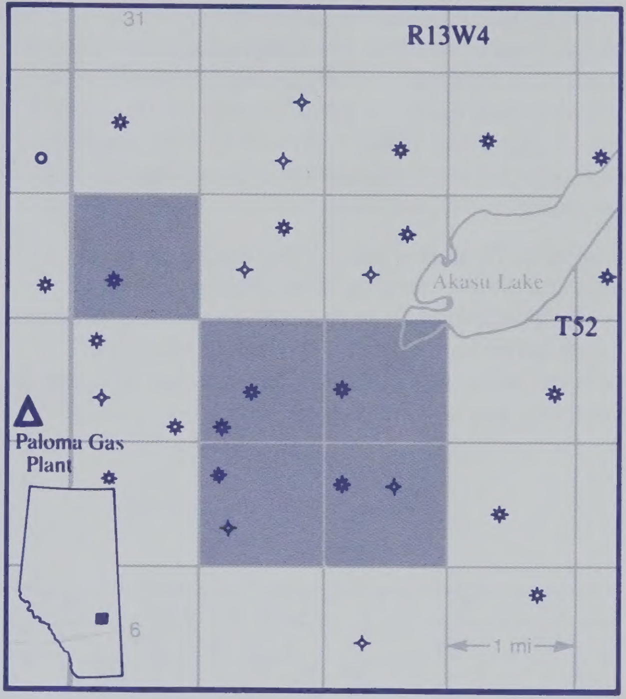


Plain Area, Alberta

Canadian Pioneer owns varying interests in three producing and three shut-in gas wells in the Plain area, which is the Corporation's largest gas producing property. The gas reserves in this area are marketed through TransCanada PipeLines Limited.

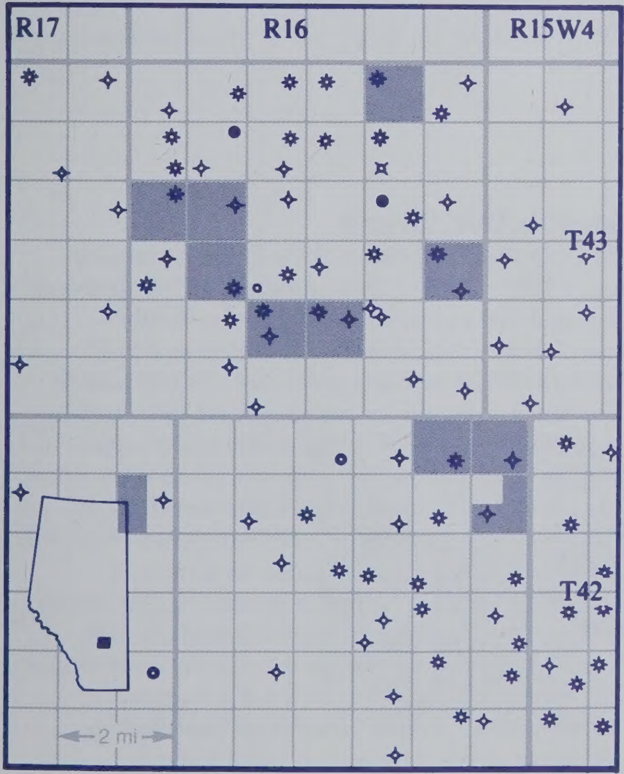
The 6-19-52-13W4M and 13-8-52-13W4M gas wells, in which the Corporation owns a 37.5% working interest, produced at average rates of 600 and 335 thousand cubic feet per day, respectively in 1986. The 6-17-52-13W4M well, in which the Corporation has a 25% working interest, produced at an average rate of 550 thousand cubic feet per day in 1986.

During 1986 Canadian Pioneer participated for a 25% working interest in the drilling of the 4-17-52-13W4M well. This Basal Quartz gas well will be placed on production in November, 1986.



PLAIN AREA, Alberta

CANADIAN PIONEER Land
Location
Gas Well
Dry & Abandoned Well



STROME AREA, Alberta

CANADIAN PIONEER Land
Location
Oil Well
Gas Well
Dry & Abandoned Well

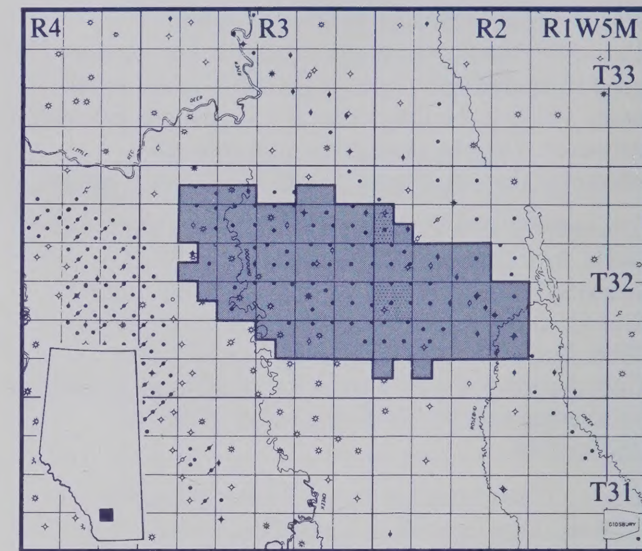
Strome Area, Alberta

In the Strome area, which is Canadian Pioneer's second largest gas producing property, the Corporation owns varying interests in four producing and three shut-in gas wells. The 1-17-43-16W4M well in which the Corporation owns a 16.25% working interest produced at an average rate of 2 million cubic feet per day during 1986. The 2-35-42-16W4M (24.7% working interest) produced at 760 thousand cubic feet per day. Two other wells in which Canadian Pioneer has gross overriding royalty interests until payout are also producing. The gas reserves in this area are sold through TransCanada PipeLines Limited.

Harmattan East Area, Alberta

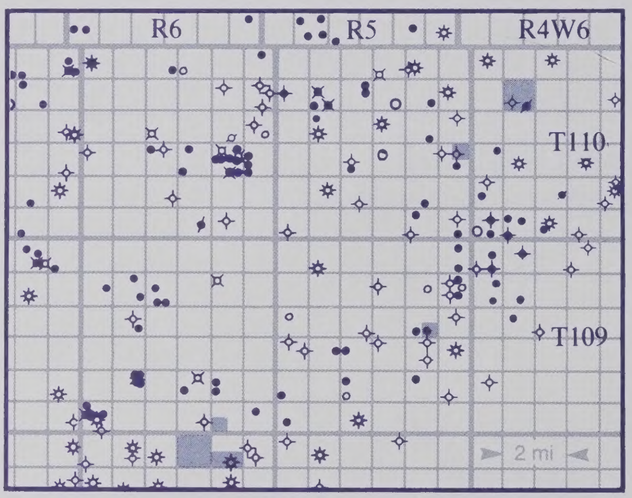
As of October 1, 1986, the Corporation's five producing oil wells in the Garrington area of Alberta have been included in the newly formed Harmattan East Viking Unit No. 1. This property remains as the Corporation's largest oil producing property.

Canadian Pioneer owns a 0.9% working interest in this unit which contains 68 producing Viking oil wells. Production from the unit is expected to exceed 3,000 barrels per day as a secondary recovery scheme utilizing a waterflood to increase ultimate oil recovery has now been implemented.

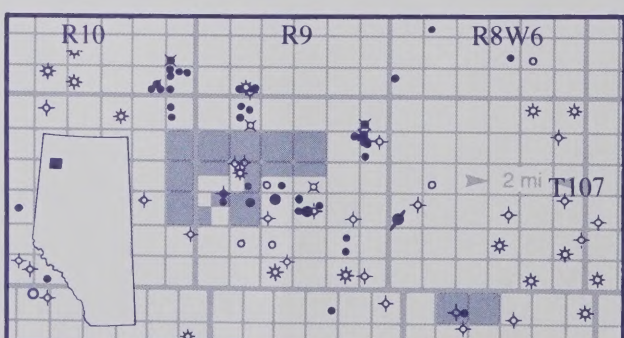


HARMATTAN EAST AREA, Alberta

CANADIAN PIONEER Land
Viking No. 1 Unit Outline
Location
Oil Well
Gas Well
Oil & Gas Well
Dry & Abandoned Well
Abandoned Oil/Water Injection



N.E. RAINBOW AREA, Alberta



S.W. RAINBOW AREA, Alberta

CANADIAN PIONEER Land
Location
Oil Well
Gas Well
Oil & Gas Well
Dry & Abandoned Well
Abandoned Oil/Water Injection

Rainbow Area, Alberta

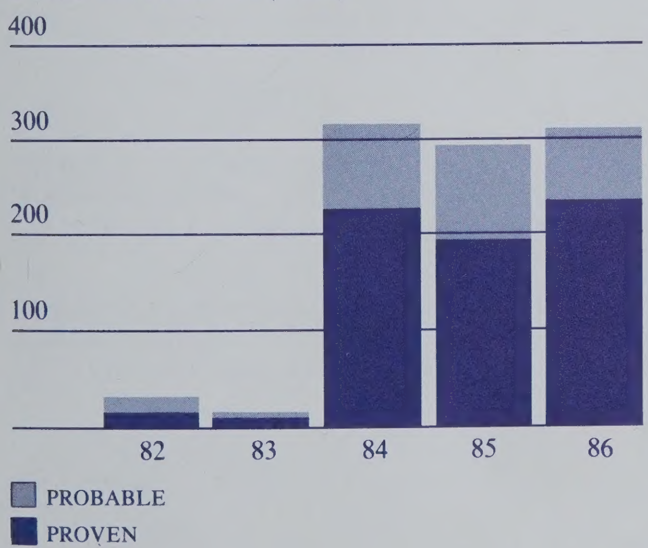
The Corporation owns working interests ranging from 1.8% to 2.8% in three producing Keg River oil wells and one potential oil well in the Rainbow area. Three of the oil wells are very prolific. The 2-23-109-5W6M well has produced 173,000 barrels of oil since going on stream in August 1983, and is currently producing at a rate of 200 barrels per day. The 2-20-107-9W6M well, which went on stream in June 1982, has produced 304,000 barrels of oil, and is producing at a rate of 225 barrels per day. The 9-18-107-9W6M well was placed on stream in August 1983, and is currently producing 300 barrels per day, with cumulative production of 262,000 barrels. The recently drilled 16-17-107-9W6M well in which the Corporation owns a 1.8% working interest will be completed as an oil producer in November, 1986. This well is expected to produce at approximately 200 barrels of oil per day.

Reserves

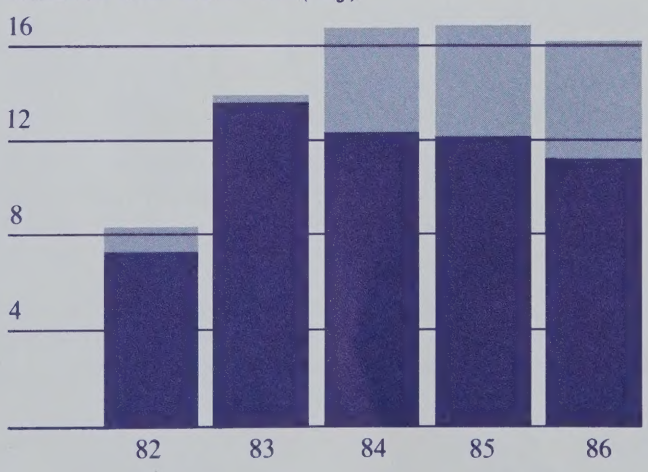
Canadian Pioneer's major oil and gas properties, representing approximately 70 percent of the Corporation's total reserves, were evaluated at September 1, 1986 by Coles Nikiforuk Pennell Associates Ltd., an independent engineering consulting firm. The minor properties, which represent about 30 percent of total reserves, were evaluated in-house by adjusting previous consultant evaluations to reflect subsequent production and reservoir performance. Reserves changed very little from 1985 to 1986 with a 15 percent increase in proven oil reserves and a seven percent decrease in proven gas reserves.

	Reserves Before Royalties					
	Canada		United States		Total	
	Oil MSTB	Gas BCF	Oil MSTB	Gas BCF	Oil MSTB	Gas BCF
1986						
Proven	201.1	10.3	29.5	1.0	230.6	11.3
Probable	56.7	4.4	19.6	0.6	76.3	5.0
Proven and Probable	257.8	14.7	49.1	1.6	306.9	16.3
1985						
Proven	163.4	10.9	36.3	1.2	199.7	12.1
Probable	77.2	4.4	16.6	0.5	93.8	4.9
Proven and Probable	240.6	15.3	52.9	1.7	293.5	17.0

Crude Oil Reserves (mstb)



Natural Gas Reserves (bcf)



Financial Review

Canadian Pioneer exhibited significant endurance throughout the 1986 fiscal year. Despite a 60 percent drop in oil prices and downward pressure on gas prices, the Corporation's net production revenue decreased only 9 percent to $2,786,000 in 1986 from $3,055,000 in 1985. An increase in production volumes helped sustain the revenue stream. However, the decrease in revenues affected cash flow from operations which decreased to $778,000 in 1986 down 24 percent from $1,029,000 in 1985.

Production expenses increased to $689,000 in fiscal 1986 from $630,000 in 1985 because of the higher gas production. General and administrative expenses decreased by $18,000 to $579,000. With lower bank debt and interest rates, interest expense decreased from $739,000 in 1985 to $661,000 in 1986.

As a result of depressed prices and markets the Corporation wrote down the book value of its United States oil and gas properties by $2,593,000 and, as a result, net earnings decreased from $328,000 (or $0.03 a share) in 1985 to a loss of $2,181,000 (or $0.21 a share) for 1986.

During the year the Corporation issued 435,330 flow through common shares for total proceeds of $441,000. The Corporation has also agreed to issue an additional 346,514 flow through common shares for a total of $175,000 by December 31, 1986.

At June 30, 1986, long term debt amounted to $5,400,000, down from $6,150,000 at June 30, 1985. The Corporation's bank is currently reviewing the loan base and in view of lower product prices a revised repayment schedule may be negotiated later in the year.

Auditors' Report

To the Shareholders of
Canadian Pioneer Oils Ltd.

We have examined the consolidated balance sheet of Canadian Pioneer Oils Ltd. as at June 30, 1986 and the consolidated statements of earnings, deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at June 30, 1986 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Calgary, Canada
August 29, 1986

Thorne Ernst & Whinney

Consolidated Balance Sheet

ASSETS

	Year ended June 30 1986	1985
CURRENT ASSETS		
Cash	$ **42,792**	$ 18,770
Accounts receivable	**620,337**	918,428
Prepaid expenses	**10,000**	35,100
	673,129	972,298
NOTES RECEIVABLE (note 2)	**272,139**	305,293
PROPERTY, PLANT AND EQUIPMENT (note 3)	**14,180,826**	12,562,717
Accumulated depletion and depreciation	**4,929,508**	1,856,146
	9,251,318	10,706,571
	$10,196,586	$11,984,162

LIABILITIES AND SHAREHOLDERS' EQUITY

	1986	1985
CURRENT LIABILITIES		
Bank advances (note 4)	$ **250,000**	$ —
Accounts payable and accrued liabilities	**827,947**	472,952
Current portion of long term debt	**250,000**	—
	1,327,947	472,952
LONG TERM DEBT (note 5)	**5,400,000**	6,150,000
DEFERRED PRODUCTION REVENUE	**333,898**	413,753
SHAREHOLDERS' EQUITY		
Capital stock (note 6)		
21,000 First Preference shares, Series A	**505,613**	505,613
8,000 First Preference shares, Series B	**200,000**	200,000
10,890,277 Class A voting common shares (1985 — 10,454,947)	**6,689,634**	6,249,097
	7,395,247	6,954,710
Deficit	**(4,260,506)**	(2,007,253)
	3,134,741	4,947,457
	$10,196,586	$11,984,162

APPROVED BY THE BOARD

J. H. Coleman
James H. Coleman — Director

John F. Kearney
John F. Kearney — Director

Consolidated Statement of Earnings

	Year ended June 30 1986	1985
Revenue		
Sale of oil and gas	**$ 2,786,318**	$ 3,055,580
Expenses		
Production	**689,106**	630,147
General and administrative	**579,014**	596,775
Interest on long-term debt	**626,486**	738,869
Other interest	**34,303**	—
Depletion and depreciation	**3,038,162**	761,497
	4,967,071	2,727,288
Earnings (loss) before income taxes and extraordinary item	**(2,180,753)**	328,292
Deferred income taxes	**—**	75,200
Earnings (loss) before extraordinary item	**(2,180,753)**	253,092
Extraordinary item		
Income tax reduction on application of prior years' losses	**—**	75,200
NET EARNINGS (LOSS)	**$(2,180,753)**	$ 328,292
NET EARNINGS (LOSS) PER COMMON SHARE		
Earnings (loss) before extraordinary item	**$(.21)**	$0.02
Net earnings (loss)	**$(.21)**	$0.03

Consolidated Statement of Deficit

	Year ended June 30 1986	1985
Deficit at beginning of year	**$(2,007,253)**	$(2,280,980)
Net earnings (loss)	**(2,180,753)**	328,292
Dividends on preference shares	**(72,500)**	(54,565)
DEFICIT AT END OF YEAR	**$(4,260,506)**	$(2,007,253)

Consolidated Statement of Changes in Financial Position

	Year ended June 30	
	1986	1985
CASH PROVIDED BY (USED FOR) OPERATIONS		
Net earnings (loss) before extraordinary item	**$(2,180,753)**	$ 253,092
Items not involving cash		
Depletion and depreciation	**3,038,162**	761,497
Deferred income taxes	**—**	75,200
Deferred production revenue	**(79,855)**	(60,539)
	777,554	1,029,250
Change in non-cash operating working capital	**678,186**	(774,949)
	1,455,740	254,301
FINANCING		
Notes receivable	**33,154**	(285,293)
Long term debt	**(500,000)**	500,000
Issue of Class A Common shares	**440,537**	645,728
Dividends	**(72,500)**	(54,565)
	(98,809)	805,870
INVESTMENTS		
Additions to property, plant and equipment	**(1,630,918)**	(1,270,679)
Proceeds on sale of equipment	**48,009**	77,000
	(1,582,909)	(1,193,679)
DECREASE IN CASH POSITION	**225,978**	133,508
Cash position at beginning of year	**18,770**	152,278
CASH POSITION AT END OF YEAR	**$ (207,208)**	$ 18,770
Cash position is comprised of:		
Cash	**$ 42,792**	$ 18,770
Bank advances	**(250,000)**	—
	$ (207,208)	$ 18,770

Notes to Consolidated Financial Statements

Year Ended June 30, 1986

GENERAL

The Company is incorporated under the Alberta Business Corporations Act and its principal business activities include the exploration, development, production and acquisition of oil and gas in Canada and the United States.

SUMMARY OF SIGNIFICANT POLICIES

Consolidation

The consolidated financial statements include the accounts of Canadian Pioneer Oils Ltd. and its subsidiary companies, all of which are wholly owned.

Petroleum and Natural Gas Operations

The Company follows the full cost method of accounting for petroleum and natural gas operations whereby all costs of exploring for and developing petroleum and natural gas reserves are capitalized on a country by country basis. Costs include land acquisition costs, geological and geophysical expenditures, carrying charges on non-producing property, costs of drilling both productive and non-productive wells, related overhead expenditures and capitalized interest related to major development projects.

Capitalized costs are limited to an amount equal to the estimated future net revenues from proved reserves, based on current prices and costs, plus the lower of cost or estimated fair value of unproved properties and major development projects. The aggregate of such future net revenues and unproved properties and major development projects for all cost centres is further reduced by estimated future aggregate general and administrative expenses, financing costs and income taxes.

Gains or losses are recognized upon the sale or disposition of property when the petroleum and natural gas reserves of the property are significant in relation to the Company's total reserves in the cost center.

Depletion and Depreciation

Depletion and depreciation of petroleum and natural gas properties, plant and equipment is provided using the unit of production method based upon estimated proved reserves as determined by the Company and independent consultants. Costs of unproved properties and major development projects are excluded from the depletion calculation until it is determined whether proved reserves exist, major development projects are complete, or impairment occurs. In calculating depletion and depreciation, crude oil reserves are converted to equivalent units of natural gas based on the relative energy content of each product.

Depreciation of property, plant and equipment is provided using a declining balance basis over the estimated life of each asset at annual rates varying from 10% to 30%.

Foreign Currency Translation

Financial statements of foreign subsidiaries are translated as follows:

(i) Monetary assets and liabilities at year-end exchange rates; all other assets and liabilities at historical rates.

(ii) Revenue and expense items are translated at average rates prevailing during the year except for depletion and depreciation which are translated at historical rates.

Exchange gains or losses, other than those resulting from long term debt, are included in the determination of net income for the year. Exchange gains or losses resulting from long term debt are deferred and amortized over the repayment period of the liability.

Joint Venture Accounting

The Company accounts for its joint venture activities using the proportionate consolidation method.

1. *Change in Accounting Policy*
Prior to July 1, 1985 the Company's aggregate capitalized petroleum and natural gas costs were limited to the future net revenues from estimated production of proved reserves at current prices and costs, plus the lower of cost or estimated fair value of unproved properties.

Effective July 1, 1985 the Company changed its accounting policy and has adopted on a retroactive basis the recommendations as set forth by the Canadian Institute of Chartered Accountants. Under this policy, the capitalized costs of all cost centres are further reduced by estimated future aggregate general and administrative expenses, financing costs and income taxes. The effect on results of this change in policy is not significant.

2. *Notes Receivable*

	1986	1985
Non-interest bearing repayable in annual instalments of $33,000 on January 1 of each year	$132,000	$165,000
Interest bearing at 10% due January 1, 1990	100,000	100,000
Non-interest bearing, payable on demand	40,139	40,293
	$272,139	$305,293

3. *Property, Plant and Equipment*

	1986			1985
	Cost	Accumulated Depletion and Depreciation	Net	Net
Petroleum and natural gas leases and rights including exploration, development and equipment thereon	$14,076,873	$4,903,619	$9,173,254	$10,627,074
Other equipment	103,953	25,889	78,064	79,497
	$14,180,826	$4,929,508	$9,251,318	$10,706,571

The costs of unproved properties excluded from the depletion computation at June 30, 1986 are $1,391,000 (1985 — $1,811,000).

During the year ended June 30, 1986 overhead expenditures of $252,000 (1985 — $250,000) have been capitalized in accordance with the accounting policy of the Company.

4. *Bank Advances*

Bank advances are available to a maximum of $500,000 and are secured by accounts receivable.

5. *Long-Term Debt*

	1986	1985
Bank loan	$5,650,000	$6,150,000
Less amount due within one year	250,000	—
	$5,400,000	$6,150,000

The revolving term bank loan is available to a maximum of $5,700,000 until October 3, 1986, the date of the annual loan review by the Company's bank. Based upon the existing loan agreement and the balance outstanding at June 30, 1986 the estimated payments until maturity are as follows: 1987 — $250,000, 1988 — $850,000, 1989 — $1,000,000, 1990 — $1,000,000, 1991 — $1,000,000, 1992 — $1,550,000.

6. *Capital Stock*

Authorized

8,000,000	First preference shares with a stated capital of $25 per share, issuable in series, of which 100,000 shares have been designated as Series A 10% cumulative, redeemable, non-voting, convertible first preference shares and 20,000 have been designated as Series B 10% cumulative, redeemable, retractable, non-voting, convertible preference shares.
20,000,000	Second preference shares with a stated capital of $10 per share, issuable in series.
100,000,000	Class A voting common shares without nominal or par value.

Issued and to be issued	Class A Common	
	Number of Shares	Consideration
Balance June 30, 1984	9,882,670	$5,803,369
Issued		
For cash	275,000	165,000
For flow through exploration expenditures	72,597	121,963
For services rendered	224,680	158,765
Balance June 30, 1985	10,454,947	6,249,097
Issued		
For flow through exploration expenditures	435,330	440,537
Balance June 30, 1986	10,890,277	$6,689,634

In February 1986 the Company agreed to issue up to 594,024 flow through Class A common shares at $0.505 per share. At June 30, 1986 247,510 shares have been issued pursuant to this agreement. The proceeds of these share issues have been committed exclusively for petroleum and natural gas exploration purposes in Canada in 1986. The purchaser of the shares acquires the rights to any related income tax benefits arising from the expenditures.

Preference Shares

The First Preference shares, Series A may be converted at any time up to June 30, 1988, at the option of the holder, into Class A common shares of the Company. The conversion price was $3.00 per Class A common share until June 30, 1985 and thereafter increased to $3.50 per Class A common share. Dividends on First Preference shares, Series A are payable quarterly. These shares are non-voting unless the Company has failed to pay dividends for six consecutive quarters. As of June 30, 1986 there are no dividends in arrears.

The Company may redeem the First Preference shares, Series A at any time provided that the current market price of the Class A common shares on the date of notice of redemption exceeds 130% of the conversion price then in effect. The First Preference shares, Series A were redeemable at $26.25 per share to June 30, 1986, thereafter declining annually by $0.25 until June 30, 1991. The Company has agreed to redeem and cancel 1½% of the issued and outstanding First Preference shares, Series A quarterly, commencing July 1, 1986.

The First Preference shares, Series B may at any time, at the option of the holder be converted to Class A common shares at a rate of 44 Class A common shares for one First Preference share, Series B. The holder may require the Company to repurchase or the Company may redeem the shares at any time at $25.00 per share together with any declared and unpaid dividends.

Warrant

A warrant entitling the holder to acquire up to 150,000 Class A common shares at $2.00 per share expires on September 30, 1986.

Stock Option Plan

As at June 30, 1986 options to purchase 775,000 Class A common shares are outstanding, exercisable from time to time to November 1989 at $0.60 per share.

7. *Income Taxes*

The income tax provisions in 1986 and 1985 differ from the amounts that would have resulted had the Canadian federal statutory tax rate been applied to the earnings (loss) before income taxes and extraordinary item, as follows:

	1986		1985	
	Amount	Percent of Pre-Tax Earnings	Amount	Percent of Pre-Tax Earnings
Computed income tax expense (recovery) at statutory rate	$(1,003,146)	(46)	$ 151,014	46
Increase (decrease) in income taxes resulting from:				
Non-deductible crown charges	110,036	5	223,244	68
Alberta Royalty Tax Credit	(58,354)	(3)	(93,064)	(28)
Resource allowance	(83,031)	(4)	(161,345)	(49)
Losses not currently utilized	1,034,495	48	—	—
Earned depletion	—	—	(18,745)	(6)
Other	—	—	(25,904)	(8)
	$ —	—	$ 75,200	23

At June 30, 1986 the Company and its subsidiaries have United States tax losses carry forward and Canadian unclaimed costs for income tax purposes of approximately $6,563,000 and $8,396,000, respectively.

8. *Segmented Information*

The Company is primarily engaged in one industry, petroleum and natural gas exploration, development and production. Information respecting the Company's operations by geographic segment is summarized as follows:

	1986		
	Canada	United States	Total
Sale of oil and gas	$2,223,117	$ 563,201	$ 2,786,318
Operating profit (loss)	$1,241,026	$(2,181,976)	$ (940,950)
General and administrative			(579,014)
Interest			(660,789)
Earnings (loss) before income taxes and extraordinary item			$ (2,180,753)
Identifiable assets			
Property, plant and equipment	$8,266,035	$ 965,310	$ 9,251,318
Other	894,160	71,081	945,268
	$9,160,195	$ 1,036,391	$ 10,196,586

	1985		
	Canada	United States	Total
Sale of oil and gas	$2,460,050	$ 595,530	$ 3,055,580
Operating profit	$1,602,477	$ 61,459	$ 1,663,936
General and administrative			(596,775)
Interest			(738,869)
Earnings before income taxes and extraordinary item			$ 328,292
Identifiable assets			
Property, plant and equipment	$7,207,966	$ 3,498,605	$ 10,706,571
Other	1,162,521	115,070	1,277,591
	$8,370,487	$ 3,613,675	$ 11,984,162

9. ***Comparative Figures***

During the year the Company changed its definition of funds from working capital to cash. The 1985 figures have been reclassified to conform with the financial presentation adopted for 1986.

Corporate Information

Directors

Sylvester P. Boland
Dublin, Ireland
Executive Vice-President
Northgate Exploration Limited

James H. Coleman* +
Calgary, Alberta
Barrister & Solicitor
Partner, Macleod Dixon

Perry S. Davids*
Calgary, Alberta
President
Palm Gas & Oil Accounting Ltd.

Patrick D. Downey
Toronto, Ontario
Vice-President & Controller
Northgate Exploration Limited

David H. Erickson +
Calgary, Alberta
Vice-President Exploration
Canadian Pioneer Oils Ltd.

Patrick J. Hughes
Dublin, Ireland
Chairman of the Board
Northgate Exploration Limited

John F. Kearney* +
Toronto, Ontario
Executive Vice-President
Northgate Exploration Limited
President & Chief Executive Officer
Canadian Pioneer Oils Ltd.

Thomas C. Riddell
Calgary, Alberta
Vice-President Land & Secretary
Canadian Pioneer Oils Ltd.

* Members of the Audit Committee
\+ Members of the Executive Committee

Officers and Corporate Management

Patrick J. Hughes
Mining Executive
Chairman of the Board

John F. Kearney
Lawyer
President & Chief Executive Officer

Patrick D. Downey
Chartered Accountant
Vice-President & Treasurer

David H. Erickson
Professional Geologist
Vice-President Exploration

Thomas C. Riddell
Petroleum Landman
Vice-President Land & Secretary

Subsidiary Companies

Frontier Canadian Oils
American Pioneer Oils Ltd.

Offices

Executive and Head Office
1701, 715 - 5th Avenue S.W.
Calgary, Alberta T2P 2X6
Telephone: (403) 265-9471
Telecopier: (403) 294-1228

Toronto Office
Suite 2701, P.O. Box 143
1 First Canadian Place
Toronto, Canada M5X 1C7
Telephone: (416) 362-6683
Telex: (06) 217766

Vancouver Office
Suite 940
800 West Pender Street
Vancouver, B.C. V6C 2V6
Telephone: (604) 682-5601

Registrar and Transfer Agent

The Canada Trust Company
505 - 3rd Street S.W.
Calgary, Alberta T2P 3Y8

Auditors

Thorne Ernst & Whinney
1200, 205 - 5th Avenue S.W.
Calgary, Alberta T2P 4B9

Legal Counsel

Macleod Dixon
1500, 324 - 8th Avenue S.W.
Calgary, Alberta T2P 2Z2

Bankers

The Bank of British Columbia

Stock Exchange Listing

The Alberta Stock Exchange
Share Symbol "CPO"

MCARA
PRINTING
LIMITED
Calgary, Alberta, Canada